MALAYSIA NATIONAL INSURANCE BHD & ANOR *a*

v.

SURUHANJAYA SYARIKAT MALAYSIA & ANOR

HIGH COURT MALAYA, KUALA LUMPUR *b*
RAMLY ALI J
[ORIGINATING SUMMONS NO: D5-24-117-2004]
17 SEPTEMBER 2004

COMPANY LAW: *Charges - Registration - Charge over reinsurance proceeds - Whether registrable under s. 108 Companies Act 1965 - Whether court has power to expunge such charge - Companies Act 1965, s. 108(3)(f)* *c*

The plaintiffs were insurance companies that issued Hull and Machinery policies over vessels ('the said policies'). They were approached by their clients, MISC, to co-issue the said policies over some vessels owned by the subsidiaries of MISC. The plaintiffs themselves would, in due course, reinsure the said policies with reinsurers to spread the risk of the insurance issued by them. To purchase the vessels, MISC had sought finance from a consortium of banks represented by the 2nd defendant, and as a condition of such finance, the 2nd defendant required that, in the event there was a claim under the insurance, the reinsurers pay the 2nd defendant directly (instead of paying the plaintiffs first, which would then in turn pay the claim to the 2nd defendant). Accordingly, an assignment of reinsurance proceeds was created. The 2nd defendant took the view that the said assignment was by way of a charge, and after the plaintiffs had signed documents and forms relating to charges under the Companies Act 1965 ('the Act'), the charge was lodged in the Registry of Charges ('the Registry') by the 1st defendant under the Act. The issues to be determined by the court were: (i) whether the charge over reinsurance proceeds ('the said charge') was registrable under s. 108 of the Act; and (ii) if not, whether the said charge which had been registered with the 1st defendant should be expunged. *d* *e* *f* *g*

h

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Held (for the plaintiffs):

[1] If at all, the said charge was only registrable under s. 108(3)(f) of the Act as a charge on book debts of the company. (p 395 f)

[1a] In the present case, what was charged was the proceeds from a contract of reinsurance *ie*, a contract of insurance over another insurance. Those proceeds could not come into being unless there was a claim under the said policies issued by the plaintiffs. Accordingly, the right charged is a right to receive the reinsurance proceeds in a contingency, which was that there should be a claim under the insurance policy first. The contract was a contingency contract. At the time the said charge was created, there was no way of knowing whether there would be any claim under the insurance policies and whether, consequently, there would be any reinsurance proceeds. Such an obligation, being wholly unascertained and unascertainable at the time the said charge was created, could not be considered a book debt. In this instance, the said charge was not a charge on book debts of the company as listed under s. 108(3)(f) of the Act, and was therefore not registrable under s. 108(1) of the Act. (pp 396 d-e & 398 c)

[2] The court has such power to expunge the said charge from the Registry on the ground that the law *ie*, s. 108 of the Act, does not require such registration of the said charge. To leave the said charge in the Registry of the 1st defendant would cause prejudice to the plaintiffs. Therefore, it was just and equitable for the court to grant relief to expunge the record of the said charge. (p 398 h)

Case(s) referred to:

Calmex Ltd v. C Lila Ltd & Ors [1989] 1 All ER 495 ***(refd)***
Coakley v. Argent Credit Corporation Plc & Ors (1998) Chancery Division ***(refd)***
Independent Automatic Sales Ltd v. Knowles & Foster [1962] 3 All ER 27 ***(refd)***
Paul & Frank Ltd & Anor v. Discount Bank (Overseas) Ltd & Anor [1967] 3 Ch 348 ***(foll)***
Pearse Farell, Liquidator of Brian Tucker Ltd (in Voluntary Liquidation) v. Equity Bank Ltd [1990] 2 IR 549 ***(foll)***
Shipley v. Marshall [1863] 14 CBNS 566 ***(refd)***

Legislation referred to:

Companies Act 1965, s. 108(1), (3)(a), (b), (c), (d), (e), (f), (g), (h), (i), (j), (k), 111
Insurance Act 1996, s. 53

For the plaintiffs - TS Oon; M/s TS Oon & Partners
For the 1st defendant - Mohd Redzuan Abdullah SFC
For the 2nd defendant - Philip Teoh; M/s Philip Teoh & Co

Reported by Suresh Nathan

JUDGMENT

Ramly Ali J:
By way of originating summons (encl. 2) the plaintiffs seek the determination of the court on the following questions, namely:

(1) Whether, upon a true construction of s. 108 of the Companies 1965 (the "Act"), a charge over the proceeds of a Reinsurance Contract constituted by a Deed of Assignment of Reinsurance Proceeds dated 8 April 2003 is a charge under s. 108(3) of the Act, and in particular s. 108(3)(f) of the Act which is subject to the requirement of registration under s. 108(1) of the Act;

(2) If the answer to the question in para. 1 is "No", that the registration of a charge in favour of the 1st defendant as Security Agent registered as Charge no. 001 on or about 8 April 2003 against the 1st plaintiff be expunged from the Registry of Charges kept by the Registrar of Companies under s. 111 of the Act;

(3) That the costs of the action be provided for; and

(4) Such further or other relief which the court shall deem fit and just.

Background Of The Case
The plaintiffs are insurance companies which issue Hull and Machinery Policies over vessels. The plaintiffs were approached by their clients, MISC to co-issue Hull and Machinery policies over some vessels owned by the subsidiaries of MISC. In due course the plaintiffs themselves would re-insure the Hull and Machinery insurance policies with reinsurers to spread the risk of the insurance issued by them. In the event of any claim on the insurance, the plaintiffs would firstly pay the owners of the vessels. The plaintiffs would then recoup any payment from the reinsurers to the extent of the reinsurance.

To purchase the vessels, MISC had sought finance from a consortium of banks represented by the 2nd defendant. As a condition of such finance, the 2nd defendant required that, in the event there was a claim under the insurance, the reinsurers pay the 2nd defendant directly (instead of paying the plaintiffs first, which would then in turn pay the claim to the 2nd defendant). Accordingly an Assignment of Reinsurance Proceeds was created.

The 2nd defendant and their solicitors took the view that the Assignment of Reinsurance Proceeds was by way of a charge. The plaintiffs were asked to and did sign, together with other documents, forms relating to charges under the Companies Act 1965 at the Registry of Companies. According to the plaintiffs, this was done in haste and without the plaintiffs obtaining independent legal advice.

The charge was lodged as "open charges" in the Registry of Companies by the 1st defendant under the Companies Act 1965.

Issues

The issues to be determined by the court are:

(1) Whether the said charge over reinsurance proceeds is registrable under s. 108 of the Companies 1965; and

(2) If the answer is 'No', whether the said charge which had been registered with the 1st defendant should be expunged.

Findngs Of Court

Section 108(1) of the Companies Act 1965 provides that where a charge to which the section applies is created by a company, there shall be lodged with the Registrar of Companies for registration within 30 days after the creation of the charge a statement of the prescribed particulars and if the section is not complied with in the relation to the charge, the charge shall, so far as any security of the company's property or undertaking is thereby conferred, be void against the liquidator or any creditor of the company.

Not all charges created by a company are subject to the requirement of registration. Only charges described in s. 108(3) of the Act are subject to such registration.

Section 108(3) of the Act provides that charges to which the section applies are:

(a) a charge to secure any issue of debentures;

(b) a charge on uncalled share capital of a company;

(c) a charge on shares of a subsidiary of the company which are owned by the company;

(d) a charge or an assignment created or evidenced by an instrument which if executed by an individual within West Malaysia and affecting property within West Malaysia would be invalid or of limited effect if not filed or registered under the Bills of Sale Ordinance 1950;

(e) a charge on land wherever situated or any interest therein;

(f) a charge on book debts of the company;

(g) a floating charge on the undertaking or property of a company;

(h) a charge on calls made but not paid;

(i) a charge on a ship or aircraft or any share in a ship or aircraft;

(j) a charge on goodwill, on a patent or licence under a patent, on a trade mark; or on a copyright or a licence under a copyright; and

(k) a charge on the credit balance of the company in any deposit account

In order to say that a charge over reinsurance proceeds is registrable, the court must be satisfied that it comes under any one of the type of charges prescribed under s. 108(3) of the Act. The nearest we can consider the charge over reinsurance proceeds is in the light of s. 108(3)(f) – ie, as a charge on book debts of the company. The said charge over reinsurance proceeds obviously does not fall under any of the other types of charges as listed under s. 108(3)(a) to (e) and (d) to (k). If at all, the said charge is registrable, then it is only registrable under s. 108(3)(f) of the Act as a charge on book debts of the company. Therefore, the issue now is to determine whether the said charge over reinsurance proceeds can be considered as a charge on book debts of the company.

"Reinsurance" is insurance over another insurance. Insurance companies normally re-insure insurance policies issued by them for the purpose of spreading the risk of the insurance issued by them. A "book debt" has been defined in many ways. In *Paul & Frank Ltd. & Anor v. Discount Bank (Overseas) Ltd. & Anor* [1967] 3 Ch 348 (1966) 2 All ER 922, the court stated some definitions of a book debt. The first definition referred to in that case was from the decision of the Common Pleas Divisional Court in *Shipley v. Marshall* [1863] 14 CBNS 566; 32 LJCP 258; 8 LT 430; 143 ER 567; 5 Digest (Rep 1) 1038, 8386. In that case *(Shipley v. Marshall)* Erle CJ defined "book debts" by saying:

> By 'book debts', the legislature doubtless intended to describe debts in some way connected with the trade of the bankrupt; and I am inclined to give the term wider range. But it is enough to say that this was a debt connected with a growing out of the Plaintiff's trade.

The second definition referred to was from the decision of Buckley J in *Independent Automatic Sales Ltd. v. Knowles & Foster* [1962] 3 All ER 27. In that case *(Independent Automatic Sales)* Buckley J said:

> So far as I am aware, no more precise definition of the meaning of the term 'book debts' has ever been attempted judicially and I shall not attempt one. *Shipley v. Marshall* n(9), I think, establishes that, if it can be said of a debt arising in the course of a business and due or growing due to the proprietor of that business that such a debt would or could in the ordinary course of such a business be entered in well-kept books relating to that business, that debt can properly be called a book debt whether it is in fact entered in the books of the business or not.

In the present case, what is charged are the proceeds from a contract of reinsurance. Those proceeds cannot come into being unless there is a claim under the Hull and Machinery Insurance Policy issued by the plaintiffs. Accordingly the right or thing charged is a right to receive the reinsurance proceeds in a contingency which is that there should be a claim under the insurance policy first. The contract is a contingency contract. At the time the charge was created, there was no way of knowing whether there will be any claim under the insurance policies and consequently whether there will be any reinsurance proceeds. Such obligation, being wholly unascertained and unascertainable at the time the charge was created cannot be considered as a book debt.

In *Paul & Frank Ltd.* the court held that the E.G.G. policy would not, in practice, be entered as a book debt before the admission of liability and the ascertainment of the amount. The court even further held that it would not in practice, be entered as a book debt even after the admission of liability and the ascertaiment of the amount.

The parties before the court are not able to cite any case on point in relation to reinsurance proceeds. However there are cases in relation to insurance proceeds and refund of insurance premiums.

The court is of the view that in principle, reinsurance proceeds and insurance proceeds have the same character.

A reinsurance contract is no more than a specialised form of an insurance contract, being an insurance of an insurance policy.

In *Paul & Frank Ltd, (supra)* an assignment of insurance proceeds by way of security was the subject matter of the claim. The liquidator of the company (in that case) sought to declare the assignment void as against the liquidator as the charge was not registered. The court held that the test of whether the insurance proceeds was to be considered a book debt was to look at the character of the obligation at the date of creation of the charge. The court held:

> ... I do not think that in ordinary speech one would describe as a book debt the right under a contingency contract as that right stands before the contingency happens. By "contingency contract" in this connexion I mean contracts of insurance, guarantee, indemnity and the like ...

At the time of the creation of the charge, it could not be said that such a debt existed (as the contingency ie, the claim under the insurance policy had not occurred). The court held that such a debt, if any, being unascertained and unascertainable could not be a book debt. Pennycuick J in that case held:

> It seems to me that, in order to ascertain whether any particular charge is a charge on book debts within the meaning of the section, one must look at the items of property which form the subject-matter of the charge at the date of its creation and consider whether any of those items is a book debt. In the case of an existing item of property, this question can only be answered by reference to its character at the date of creation. Where the item of property is the benefit of a contract and at the date of the charge the benefit of the contract does not comprehend any book debts, I do not see how that contract can be brought within the section as being a book debt merely by reason that the contract may ultimately result in a book debt.

In that case, the court held that the charge was not a charge on book debts on the ground that, at the date when the charge was created, no debt, or book debt, was due under the policy at all so that the charge could not have been on any book debt.

In *Coakley v. Argent Credit Corporation Plc. and Ors.* (1998) Chancery Division, the court took a similar view regarding charges over the proceeds of two insurance policies. Rimer J in that case applying the principles as established *Paul & Frank Ltd, Independent Automatic Sales* and *Shipley v. Marshall (supra)* held:

Applying the principles established by the above authorities, I approach the present case on the basis that a book debt is a debt arising in the course of a business and being such as is commonly entered in well-kept books relating to the business.

The same conclusion was reached in *Pearse Farrell, Liquidator of Brian Tucker Limited (in Voluntary Liquidation) v. Equity Bank Limited* [1990] 2 IR 549, in relation to refunds of insurance premiums.

Applying the above authorities the court is of the view that the charge over reinsurance proceeds in the present case is not a charge on book debts of the company as listed under s. 108(3)(f) of the Companies Act 1965. It is therefore not registrable under s. 108(1) of the Act. That being the case, the plaintiffs are not required to register the charge with the 1st defendant (the Companies Commission, Malaysia) and the 1st defendant is not duty bound to record the charge in it's register.

As a matter of fact, the charge had been registered with the 1st defendant. The plaintiffs have deposed to the prejudice which has been caused to them as a result of the record of the charge being kept and maintained at the registry of the 1st defendant. One of the prejudice is the possibility of an enquiry as to whether there is a breach under s. 53 of the Insurance Act which prohibits the granting of a charge over the assets of an insurance company without the permission of Bank Negara Malaysia (BNM). This is a serious offence punishable by three years imprisonment or a fine of RM3 million or both.

Secondly the financial integrity of the plaintiffs is called into question. Insurance companies, as holders of public money in the form of premiums and funds managed by them cannot have their financial integrity questioned. Accordingly any record which purport to show the creation of a charge over the assets of the plaintiffs will raise questions as to the financial integrity of the plaintiffs. The plaintiffs in their entire history have never had any charges created over their assets.

Has the court any power to expunge such charge from the registry of the 1st defendant?

The court is of the view that the court has such power to expunge the charge for the register on the ground that such registration of the charge is not required by law ie, s. 108 of the Companies Act 1965 as has been deliberated earlier. To leave the charge to be in the register at the registry of the 1st defendant will cause prejudice to the plaintiffs. Therefore, it is just and equitable for the court to grant relief to expunge the record of the charge in the register as prayed by the plaintiffs.

In *Calmex Ltd. v. C. Lila Ltd & Ors* [1989] 1 All ER 495, a winding-up order was made by mistake, against the plaintiffs as there was a confusion in the court as to the name of the debtor. Accordingly, once that order was made and later recorded, a notice of the winding-up was sent to the Registrar of Companies, who then kept a record of the same. The plaintiffs upon discovering the error, applied to set aside the winding-up order and to order the registrar to expunge the record of the winding-up. The court excercised an inherent power to expunge the record of the winding-up Hoffman J said:

> Finally, counsel for the registrar submitted that the Court had no jurisdiction to tell the registrar to remove documents from the register. I would be surprised if a company had no remedy against the registrar if he chose to include in the file a document which was prejudicial to the company and which he had no statutory duty to keep. And I have held that, on the true construction of s. 130(1) of the 1986 Act, the registrar has no duty to retain entered in his records a winding-up order which the Court has declared to be a nullity. I suspect that the registrar did not wish to take any point on the procedure by which the matter has been brought before the Court, but contended that even by way of judicial review there was no jurisdiction. In my judgment the Court does in principle have jurisdiction according to ordinary public law principles to control the way in which the registrar carries out his statutory duties, subject to any specific exclusions of that jurisdiction or the evidence on which it could be founded, as in *R v. Registrar of Companies, ex p Central Bank of India* [1986] 1 All ER 105, [1986] QB 1114. I will therefore make an order that the winding-up and stay orders be removed from the registrar's files, subject, if the registrar thinks it desirable, to their replacement by a note in terms on which I shall invite the views of counsel.

Conclusion

Based on the about considerations the court held that:

(i) a charge over the proceeds of a reinsurance contract constituted by a Deed of Assignment of Reinsurance Proceeds dated 8 April 2003 is not a charge on book debts of the company and therefore not registrable under s. 108 of the Companies Act 1965;

(ii) that the registration the said charge registered as charge no: 001 on or about 8 April 2003 be expunged from the Registry of Charges kept by the 1st defendant; and

(iii) each party to bear their own costs.